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IN THE

Supreme Court of the United States

OCTOBER TERM, 1950

No. 459.

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,

Petitioner,

vs.

FEDERAL POWER COMMISSION,

Respondent,

PAN AMERICAN PETROLEUM CORPORATION, ATLANTIC REFINING COMPANY, CITIES SERVICE PRODUCTION COMPANY, HUMBLE OIL & REFINING COMPANY, OHIO OIL COMPANY, OIL PARTICIPATIONS INCORPORATED, TIDEWATER OIL COMPANY, TRANSCONTINENTAL GAS PIPE LINE CORPORATION, CONTINENTAL OIL COMPANY, MAGNOLIA PETROLEUM COMPANY, PURE OIL COMPANY, SUN OIL COMPANY, UNION OIL COMPANY OF CALIFORNIA, W. H. HUNT, TRUSTEE FOR HASSIE HUNT TRUST, PHILLIPS PETROLEUM COMPANY,

Intervenor-Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF FOR PETITIONER PUBLIC SERVICE COMMISSION IN REPLY.

PUBLIC SERVICE COMMISSION OF THE
STATE OF NEW YORK,
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Albany, New York,
December 1, 1950.

PRESS OF BYRON S. ADAMS, INC., ALBANY, N. Y., U.S.A.

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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF FOR PETITIONER PUBLIC SERVICE COMMISSION IN REPLY.

Briefs, in opposition to our petition for certiorari and for summary reversal of the judgment below, have been filed by (1) producers intervenor-respondent,* (2) the

* One of behalf of Pan American Petroleum Corporation and 10 others of the 26 producer-applicants before FPC; one on behalf of intervenor-respondent Sun Oil Company.

pipeline intervenor-respondent (Transco) and (3) the respondent Federal Power Commission (FPC).*

In different ways, each endeavors to depict the instant Catco-patterned and prompted, unconditional certification of 2½¢ per Mcf, southern Louisiana gas producer sales, as *Catco*-** blessed. In different ways, each represents that the only thing that prompted this Court to upset the Tennessee producer-suppliers' efforts to accomplish a comparable initial price elevation in *Catco* was the absence of evidence of "need" on the part of Tennessee and its customers for any additional gas supplies—an evidentiary defect not here present. In different ways, each asserts that given such evidence in a producer certificate case, the FPC may then "weigh[t]" that factor sufficiently to "counterbalance" (a) any and all deficiencies in the proof with respect to the propriety of the producer price *per se* and (b) any and all deleterious impacts upon the consumer which the price proposal may engender—and no Court may intrude. In different ways, each describes petitioner's contrary notions of the law as reflecting "misconstruction" or "misinterpretation" of the decision of this Court of June 22, 1959, which bears petitioner's name. In effect, each would relegate some 6 pages of this Court's opinion in that case—pertaining to respondent's statutory duty under Section 7 of the Natural Gas Act, when confronted with high-price producer certificate applications—to the status of *obiter dicta*.

With the respective contentions we will deal *seriatim* (*infra*). First, however, we would place before the Court what we conceive to be the heart of this Court's recent

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* Just as was the case in *Catco*, the respondent's brief is *not* signed by the Solicitor General.

** *Atlantic Refining Co., et al.* v. *Public Service Commission of New York*, 360 U. S. 378 (June 22, 1959).

pronouncement respecting (1) the producer's obligation in a Section 7 certificate case before FPC and (2) that agency's responsibilities with respect thereto—the pronouncement differing markedly from the previous* (and evidently persistent**) conceptions of the producers, the pipelines and the FPC on the subject.

"II. The Validity of the Order

The purpose of the Natural Gas Act was to underwrite just and reasonable rates to the consumers of natural gas. *Federal Power Comm'n* v. *Hope Natural Gas Co.*, 320 U. S. 591 (1944). As the original 7 (c) provided, it was 'the intention of Congress that natural gas shall be sold in interstate commerce for resale for ultimate public consumption for domestic, commercial, industrial, or any other use at the lowest possible reasonable rate consistent with the maintenance of

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* *Matter of Continental Oil Co., et al.* (Catco), 17 FPC 880 (June 24, 1957); *Matter of Southern Natural Gas Co.*, 19 FPC 558 (April 18, 1958); *Matter of Transcontinental Gas Pipe Line Corp.*, 20 FPC 264 (Op. No. 315, September 4, 1958). See brief for respondent Public Service Commission in *Atlantic Refining Co., et al.* v. *PSC*, 360 U. S. 378, at pp. 36-42. *Catco* overruled the first cited determination and, we here submit, the last as well. In addition, it mandated expeditious Section 5 rectification of the damage done by the intervening, equally defective high-price certification—a course the FPC directed but, to date, has not pursued. See Transco brief, App. E.

** *Matter of Trunkline Gas Co., et al.*, Docket No. G-1539 (Op. No. 321, May 22, 1959; rehearing rejected, July 22, 1959); *Matter of Texas Gas Transmission Co., et al.*, Docket No. G-17335, Op. No. 327 (August 10, 1959); *Matter of the California Co., et al.*, Docket No. G-16108 (August 10, 1959); *Matter of Sun Oil Co., et al.*, Docket No. G-15122 (August 10, 1959); *Matter of Sunray Mid-Continent Oil Co.*, Docket No. 14753 (August 10, 1959); *Matter of Superior Oil Co., et al.*, Docket No. G-16380 (August 10, 1959)—referred to at p. 26 of PSC petition for certiorari herein. Petitions for judicial rectification of *each* such erroneous application of *Catco* are now pending in various Courts of Appeal.

adequate service in the public interest.' 52 Stat. 825.[7] The Act was so framed as to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges. The heart of the Act is found in those provisions requiring initially that any 'proposed service, sale, operation, construction, extension, or acquisition . . . will be required by the present or future public convenience and necessity,' §7 (e), 15 U. S. C. §717f (e), and that all rates and charges 'made, demanded or received' shall be 'just and reasonable,' §4, 15 U. S. C. §717 (c). The Act prohibits such movements unless and until the Commission issues a certificate of public convenience and necessity therefor, §7 (c), 15 U. S. C. §717f (c). Section 7 (e) vests in the Commission control over the conditions under which gas may be initially dedicated to interstate use. Moreover, once so dedicated there can be no withdrawal of that supply from continued interstate movement without Commission approval. The gas operator, although to this extent a captive subject to the jurisdiction of the Commission, is not without remedy to protect himself. He may, unless otherwise bound by contract, *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U. S. 332 (1956), file new rate schedules with the Commission. This rate becomes effective upon its filing, subject to the 5-month suspension provision of §4 and the posting of a bond, where required. This not only gives the natural gas company opportunity to increase its rates where justified but likewise guarantees that the consumer may recover refunds for moneys paid under excessive increases. The overriding intent of the Congress to give full protective coverage to the consumer as to price is further emphasized in §5 of the Act, 15 U. S. C. §717d, which authorizes the Commission *sua sponte*, or otherwise, to institute an inves-

[7] The 1942 amendments to §7, 56 Stat. 83, were not intended to change this declaration of purpose. See Hearings, House Interstate and Foreign Commerce Committee, on H. R. 5249, 77th Cong., 1st Sess. 18-19; H. R. Rep. No. 1290, 77th Cong., 1st Sess.; S. Rep. No. 948, 77th Cong., 2d Sess.

tigation into existing rates and charges and to fix them at a just and reasonable level. Under this section, however, the rate found by the Commission to be just and reasonable becomes effective prospectively only. Gas purchasers, therefore, have no protection from excessive charges collected during the pendency of a §5 proceeding.

In view of this framework in which the Commission is authorized and directed to act, the initial certificating of a proposal under §7 (e) of the Act as being required by the public convenience and necessity becomes crucial. This is true because the delay incident to determination in §5 proceedings through which initial certificated rates are reviewable appears nigh interminable. Although *Phillips Petroleum Co.* v. *Wisconsin*, 347 U. S. 672, was decided in 1954, cases instituted under §5 are still in the investigative stage. This long delay, without the protection of refund, as is possible in a §4 proceeding, would provide a windfall for the natural gas company with a consequent squall for the consumers. This the Congress did not intend. Moreover, the fact that the Commission was not given the power to suspend initial rates under §7 makes it the more important, as the Commission itself says, that 'this crucial sale should not be permanently certificated unless the rate level has been shown to be in the public interest.' 17 F. P. C. 563, 575.

This is especially true where, as here, the initial price will set a pattern in an area where enormous reserves of gas appear to be present. We note that in petitioners' proof a map of the Continental Shelf area off of the cost of Louisiana shows that the leases here involved cover but 17 out of a blocked-out area covering some 900 blocks of 5,000 acres each. The potential of this vast acreage, in light of discoveries already made as shown by the record, is stupendous. The Commission has found that the transaction here covers the largest reserve ever committed to interstate commerce in a single sale. Indications are that it is

but a puff in comparison to the enormous potentials present under the seabed of the Gulf. The price certificated will in effect become the floor for future contracts in the area. This has been proven by conditions in southern Louisiana where prices have now vaulted from 17 cents to over 25 cents per M(F. New price plateaus will thus be created as new contracts are made and unless controlled will result in 'exploitation' at the expense of the consumer, who eventually pays for the increases in his monthly bill.

It is true that the Act does not require a determination of just and reasonable rates in a §7 proceeding as it does in one under either §4 or §5. Nor do we hold that a 'just and reasonable' rate hearing is a prerequisite to the issuance of producer certificates. What we do say is that the inordinate delay presently existing in the processing of §5 proceedings requires a most careful scrutiny and responsible reaction to initial price proposals of producers under §7. Their proposals must be supported by evidence showing their necessity to 'the present or future public convenience and necessity' before permanent certificates are issued. This is not to say that rates are the only factor bearing on the public convenience and necessity, for §7 (e) requires the Commission to evaluate all factors bearing on the public interest. The fact that prices have leaped from one plateau to the higher levels of another, as is indicated here, does make price a consideration of prime importance. This is the more important during this formative period when the ground rules of producer regulation are being evolved. Where the application on its face or on presentation of evidence signals the existence of a situation that probably would not be in the public interest, a permanent certificate should not be issued.

There is, of course, available in such a situation, a method by which the applicant and the Commission can arrive at a rate that is in keeping with the public convenience and necessity. The Congress, in §7 (e),

has authorized the Commission to condition certificates in such manner as the public convenience and necessity may require. Where the proposed price is not in keeping with the public interest because it is out of line or because its approval might result in a triggering of general price rises or an increase in the applicant's existing rates by reason of 'favored nation' clauses or otherwise, the Commission in the exercise of its discretion might attach such conditions as it believes necessary.

This is not an encroachment upon the initial rate-making privileges allowed natural gas companies under the Act, *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp., supra,* but merely the exercise of that duty imposed on the Commission to protect the public interest in determining whether the issuance of the certificate is required by the public convenience and necessity, which is the Act's standard in '7 applications. In granting such conditional certificates, the Commission does not determine initial prices nor does it overturn those agreed upon by the parties. Rather, it so conditions the certificate that the consuming public may be protected while the justness and reasonableness of the price fixed by the parties is being determined under other sections of the Act. Section 7 procedures in such situations thus act to hold the line awaiting adjudication of a just and reasonable rate. Thus the purpose of the Congress 'to create a comprehensive and effective regulatory scheme,' *Panhandle Eastern Pipe Line Co.* v. *Public Service Comm'n of Indiana,* 332 U. S. 507, 520 (1947), is given full recognition. And '7 is given only that scope necessary for 'a single statutory scheme under which all rates are established initially by the natural gas companies, by contract or otherwise, and all rates are subject to being modified by the Commission . . .' *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp., supra,* at 341. On the other hand if unconditional certificates are issued where the

rate is not clearly shown to be required by the public convenience and necessity, relief is limited to §5 proceedings, and, as we have indicated, full protection of the public interest is not afforded.'

Our examination of the record here indicates that there was insufficient evidence to support a finding of public convenience and necessity prerequisite to the issuance of the permanent certificates. The witnesses tendered developed little more information than was included in the printed contracts. As the proposed contract price was higher than any paid by Tennessee, including offshore production in the West Delta area of Louisiana, it is surprising that evidence, if available, was not introduced as to the relative costs of production in the two submerged areas. Moreover the record indicates that the proposed price was some 70¢ higher than the weighted average cost of gas to Tennessee; still no effort was made to give the 'reason why.' More damaging, was the evidence that this price was greatly in excess of that which Tennessee pays from any lease in southern Louisiana. Likewise the $16,000,000 pipeline to the producers' wells was unsupported by evidence of practice or custom. Respondents contend — and it stands undenied — that this alone would add 2 cents per MCF to the cost of the gas. Again the free movement of distillates retained by the producers was 'shrugged off' as being *de minimis*, without any supporting data whatever. Nor was the evidence as to whether the certification of this price would 'trigger' increases in leases with 'favored nation' clauses convincing, and the claim that it would not lead to an increase in rates by Tennessee was not only unsupported but has already proven unfounded.'

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[8] Tennessee has subsequently filed an application with the the F. P. C. requesting higher rates designed to produce some $19,000,000 additional annual revenue. Tennessee Gas Transmission Co., Docket G-17166."

(*Atlantic Refining Co.* v. *Public Service Commission*, Oct. Term, 1958, Opinion of the Court, 360 U. S. 378, pp. 388-393.)

That that discussion, pertaining as it does to the necessity for adequate demonstration of the propriety of the *initial price* aspect of the Section 7 public convenience and necessity "complex", *presupposed* the presence of adequate evidentiary support for all other aspects of that "complex"—including "need" for the gas involved on the part of the pipeline-purchaser, and through it the purchaser's distributor customers—is, we think, self-evident. When the Court then went further, in the immediately following and concluding paragraph (360 U. S. 393-4), and properly observed (because *that* point had *also* been emphasized and it was an attribute of that case): "Nor do we find any support whatever in the record for the conclusory finding on which the order was based that 'the public served through the Tennessee Gas System is greatly in need of increased supplies of natural gas' ", ***the Court did not thereby limit the scope, pertinence or import of what it had previously said with respect to the necessity for demonstration of the necessity for the initial price, to situations where evidence of the purchaser's need for the gas was missing.*** Conversely, the Court did not thereby pronounce that *with* evidence of the purchaser's need present, everything it had previously said with respect to the necessity for demonstration of the propriety of the initial price became *dicta;* it did not hold that with evidence of need, the unsupported initial price aspect of the case before the FPC could be brushed aside or "counterbalanced" away: it did not say, hold or imply that inadequately supported unconditional certificates could properly be issued, regardless of the price impact, under a conclusory rationalization

that, on balance, the consumer would not be "adversely" affected (except in his pocketbook).

Such, however, is the essence of the contentions of the opponents of the instant petition.

I.

The Producers.

The producers contend that we are in error in our impression that *Catco* imposes an obligation upon them to "justify", their initial price proposals. All *Catco* requires, we are told, is that there must be evidence *of* (not necessarily supporting) "all factors" comprising the public convenience and necessity "complex"—including the purchaser's need for gas; that with each factor *so* evidenced, the FPC's "weighing" process may then proceed, with its outcome rendered immune from judicial review. Here, we are told, each factor *was* evidenced—the evidence pertaining to price consisting of demonstration of *what* it was, there being no necessity for the producers to show *why* it was what it was. This, it is said, is adequate demonstration that "the rate-level . . . [is] . . . in the public interest" (360 U. S. 390). This, it is said, is all that this Court meant in its observation that "Their [the producers' rate] proposals must be supported by evidence showing their necessity . . ." (360 U. S. 391). When, under such circumstances, the FPC proceeds to weigh all factors and grant permanent unconditional certification of the high price sale, it is said, this constitutes "most careful scrutiny [of] and responsible reaction to initial price proposals of producers" (360 U. S. 391), notwithstanding the various deleterious aspects

(impact) to ensue from such certification. Here, we are told, the initial prices may be and properly were denominated by FPC as not "adverse" to—though to be borne entirely by—the consuming public, because, (a) the *public* needs more gas*; (b) the *distributors* will effect great "savings" in paying high prices for this gas because it would cost them even more to manufacture similar quantities**; and (c) the *producers'* entitlement thereto (or lack thereof) is immaterial because the initial price level in the marketing area has not been breached. To establish the latter, reference is made to the Cateo sales (!) and those encompassed in other Cateo-inspired certificate cases decided by FPC between June 24, 1957 (Cateo) and September 4, 1958 (this one), *before* this Court advised the producers and the FPC of their respective obligations under

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* For discussions of the pertinence of this aspect of a producer certificate case in the evaluation of the propriety of the producer's price, see brief for respondent PSC in *Cateo*, Point III, pp. 56-57; Supplemental brief of respondent PSC in *Cateo*, Point I, pp. 5-9; and (since Transco has quoted out of context therefrom—Transco brief herein at p. 21) the following excerpt from the *Cateo* oral argument before this Court:

> "Mr. Brown: It is conceivable that there might be such a screaming need for gas under some circumstances, not here present, that they could junk price and not pay attention to it and not be guided principally by it. They cannot, we believe, bargain price away under the guise of need for expansion of gas facilities.
>
> The whole purpose of regulation presupposes need for the regulated commodity and a necessity for the exercise of price regulatory supervision. You do not bargain together and weigh one against the other and junk one or the other, as you elect. You must reconcile them both. That we think the Commission failed to do in its third order."

** For demonstration of the delusive character of this prop, erected in support of the determination under review in (by) the Court below, see PSC petition herein at pp. 17-20.

the Natural Gas Act with respect to unjustified initial price spirals. (See *supra*, p. 3, fn.*).*

II.

Transco.

In its brief Transco depicts with clarity and candor the "plight" of the pipeline middle-man—the conduit from the producer to the consumer of both the gas and its total cost. On the one hand, besieged by distributor company customers with actual or potential markets for more natural gas; in its own self-interest anxious to transport more and more gas—and on the other hand, confronted with a producer-sellers' market with ever-mounting and, to date,

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* Utilization of or even reference to the 23¢ sales which were unconditionally certificated in *Southern Natural Gas Co.*, Docket No. G-13082, *et al.*, 19 F. P. C. 558 (April 18, 1958)—for this or any other purpose—is particularly appalling. In the first place, this Petitioner was denied intervention by FPC in Southern Natural's gas acquisition proceedings, upon the ground that the prices to be paid to producers by that company did not and could not, adversely or otherwise, affect our interests! (See P. S. C. Petition for Certiorari, p. 16, ftn.*). In the second place, as casual perusal of the FPC order discloses (see *verbatim* copy, Transco Brief, Appendix E) the only other potential consumer-objector to those high-priced sales was induced to withdraw from the proceedings and the applications were thereafter submitted to the FPC without hearing and hence without *any* evidence supporting *any* facet, much less the initial price aspect thereof. Finally, in certificating the sales, while Respondent observed in passing that: "These proposed prices [22.8¢ per Mcf] will be among the highest to be paid for natural gas produced in the Southern Louisiana area. In view of this fact, we will by subsequent order institute investigations pursuant to Section 5(a) of the Natural Gas Act as to the reasonableness of the prices proposed . . .", notwithstanding the passage of more than a year and a half, no such proceedings have been instituted or pursued. All of this notwithstanding, these Southern Natural certifications are now held forth (extolled) as demonstrative of the legitimate "going price line" in the area (See Transco Brief, p. 23; F. P. C. Brief, p. 10)!

unrestrained (by FPC) price demands (to be met or no sale)—the pipeline-purchaser is compelled to compete with (endeavor to out-bid) other would-be purchasers in the field. And they all are, in general, at the mercy of a handful of gigantic producer-sellers who control the bulk of the supply. In most instances the bidding starts at the level of the highest previous sale in the area. Both the seller and the purchaser are aware of the necessity for subsequent FPC certification of the sale but this imposes little or no restraint upon the full application of the "what-the-market-will-bear" bidding process because, to date, for southern Louisiana sales FPC has used as the measure of what it would certificate, precisely whatever emerged from such negotiations!

When later before FPC in quest of such certification and confronted with (1) the producer-seller's adamant refusal to justify, explain, rationalize or even comment upon his price and (2) the "pay-all-cost" consumer demanding that certification, if granted, be conditioned for his protection, the pipeline-purchaser promptly points to the likelihood of such FPC action occasioning its loss of the gas involved. Hence, in pipeline conception, the FPC's statutory price conditioning power should *never* be exercised by it in such a context. When the consumer-prompted Court review of the invariably ensuing unconditional certification is instituted, the pipeline company erects the same loss-of-gas chamber of horrors, by then buttressed by the *fait accompli* of the new pipeline facilities which were, in the interim, constructed to accommodate the subject supply. Hence, in pipeline conception, *no Court* should ever deign to reverse an FPC producer-pipeline certification because such might "jeopardize" the continuity of its gas supply

and its multi-million dollar capital expenditure made to secure it.*

Such is the content of the instant Transco presentation. It would seem obvious enough that if the *Catco*-pronounced principles of FPC certification of proposed producer interstate sales had been consistently applied in the past, the depicted pipeline "plight" would never have arisen. It would seem equally obvious that if they are consistently applied by both FPC and the Courts sitting in review of FPC certifications, now and in the future, the plight will evaporate. *All* producer-sellers seeking interstate disposition of their gas will be subject to the same requirements: i. e., (a) demonstrate the propriety of the price or (b) expect the certificate to be conditioned at a price level which will not unreasonably impinge upon the ultimate consumer. *All* interstate pipelines will be in comparable competitive positions, in this respect, as purchasers of the needed commodity.

III.

The Respondent.

The brief for respondent FPC reflects, better than we could hope to, the complete misinterpretation by the Court below of the import of *Catco* and FPC's own great relief in having *Catco* so undermined. To demonstrate:

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* Neither has been "jeopardized" for Tennessee as the result of *Catco*. (Catco gas started flowing at 22.4¢ per Mcf in June, 1958, and is still flowing, under temporary certificates conditioned as to price upon final outcome of the FPC determination upon the remand directed by this Court.) Neither is likely to be "jeopardized" for Transco by the action of this Court which is so patently called for herein.

1. *Catco*, says the FPC, held that the producer's price must be justified *either* by proof supporting it *per se*, *or* by evidence of public need for the gas involved. Here, admittedly, the former is entirely lacking, but the latter has been supplied—hence the unconditional certification meets the *Catco* test (citing the decision below and its own August 10, 1959 series of 23¢ southern Louisiana unconditional certifications granted *6 days* after release of the opinion below and expressly in reliance thereupon—*supra*, p. 3 ftn.**).

2. *Catco*, the FPC agrees, erected certain "signals" which should prompt its careful scrutiny of and responsible reaction to the producer's price proposal, namely, (a) comparison thereof with the legitimate "going price line" in the area and (b) its impact upon the purchasing pipeline, through triggering or otherwise. Here, says the FPC, the initial price proposals were "in line", in that Catco purchases and others so inspired are comparable—and whether the comparatives are legitimate or no is not material—they are factual unless and until reduced in Section 5 proceedings; here, admittedly, the impact of the instant purchases upon Transco will mean increased costs to its (Transco's) customers—but they agreed to them and, besides, their need for gas outweighs such impact and renders the latter "not adverse".

3. In two instances, says FPC, we have—in accordance with the teachings of *Catco*—exercised our price conditioning prerogatives to maintain the price level, in other than southern Louisiana fields, at or about the highest level heretofore certificated [and this has been done (temporarily) notwithstanding the presence of evidence in those two cases of urgent public need for the gas supplies involved!] Accordingly, says FPC, there is no need for

this Court to grant certiorari herein and discourse again—so soon after Catco—on the subject of Section 7 of the Natural Gas Act.

Conclusion.

With the latter portion of the FPC's presentation we are in total accord. There is no need for this Court to re-state its lucid *Catco* dissertation upon respondent's duties and obligations under Section 7 of the Natural Gas Act. There is, however, an obvious, vital need for this Court to act upon the instant petitions in such a way as to preserve the integrity of this Court's June 22, 1959 pronouncement upon the subject. This may be accomplished by grant of the applications and summary reversal of the judgment below, upon the cited authority of *Atlantic Refining Co., et al.* v. *Public Service Commission of the State of New York,* 360 U. S. 378. This, on behalf of the millions of gas consumers we represent, we respectfully urge.

Respectfully submitted,

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December 4, 1959.